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Comparative Advantage in Thailand and Indonesia and Thailand's Free Trade Agreements: Potential Diversion of Indonesian Exports

William E. James, PhD
Nathan Associates, Inc.

September 6, 2004

GROWTH THROUGH INVESTMENT, AGRICULTURE AND TRADE (GIAT)

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Abstract

This paper seeks to explore the implications of Free Trade Agreements (FTAs) between Thailand and the United States and Thailand and Japan for Indonesia's trade. In particular, Indonesia's export patterns are broadly similar to those of Thailand with these two large trading partners. A mapping of export similarities between Thailand and Indonesia in the two big markets of the United States and Japan is undertaken in order to identify sectors where trade diversion might result from one partner (Thailand) gaining preferential market access, while the other (Indonesia) is denied such access given differences between MFN and FTA tariff levels. Rules of origin used to enforce the preferential trade agreements are crucial in determining whether or not such agreements are likely to be net trade diverting or net trade creating.

Comparative Advantage in Thailand and Indonesia and Thailand's Free Trade Agreements: Potential Diversion of Indonesian Exports

Executive Summary

Thailand is in the process of negotiating free trade agreements (FTAs) with both of Indonesia's largest trading partners—Japan and the United States. Indeed, of all the ASEAN countries except Singapore, Thailand has been the most active in seeking out bilateral preferential trading agreements or FTAs. Indonesia has recently begun to study the feasibility of FTA negotiations but to date prefers to operate within the confines of the Association of Southeast Asian Nations (ASEAN). Although ASEAN has formed a free trade area under the ASEAN Free Trade Agreement (AFTA), only about 20 per cent of ASEAN members trade is within the region and, although no official figures are available, it is thought that only a small percentage of this trade takes advantage of ASEAN tariff preferences under the Common Effective Preferential Tariff (CEPT) scheme. ASEAN has announced long-term plans for FTAs with China, India, Japan and Korea, but previous efforts to link ASEAN and the Australia-New Zealand Closer Economic Relationship (CER) in an FTA did not materialize.

Because of the slow progress in the ASEAN process, Thailand has aggressively sought out bilateral treaties with the big markets. Free Trade Agreements involving Singapore are unlikely to divert significant amounts of Indonesian exports because of the differences in products produced and traded. Singapore operates with virtually zero tariffs and thus, new FTAs will carry little risk of diverting intra-ASEAN trade in Singapore. Free trade agreements involving Thailand and major markets like the U.S. and Japan, however, are of potential concern to Indonesia. This is because there is a very strong similarity in export composition between Indonesia and Thailand.

An assessment of potential trade diversion in the two major export markets resulting from Thailand obtaining preferential access while Indonesia does not is presented in this report. The top fifty non-oil exports of Indonesia (using official import statistics of the U.S. and Japan from Indonesia), accounting for over 90 percent of Indonesian non-oil exports in these markets are evaluated from the standpoint of competition with similar Thai products. In the case of Japan, 40 of the top 50 products are directly competing with Thai products and in the case of the U.S. 28 of

the top 50 are directly competing with Thai products. Over $10 billion worth of non-oil exports (over 20 percent of total non-oil exports) are at risk of trade diversion should Thailand succeed in FTA negotiations with the U.S. and Japan, with textile and apparel items among the most vulnerable to trade diversion in the markets of the U.S. and Japan.

The determining factors in whether much trade diversion is likely to occur include the difference between most-favored nation (MFN) tariffs paid by Indonesia and preferential tariffs under FTAs (the so-called "margin of preference") as well as the rules used to determine product origin and eligibility for preferential treatment. The U.S. and Japan have indicated they will proceed with negotiations with Thailand as a priority and will also pursue arrangements with Malaysia and the Philippines following those with Thailand. Indonesia could possibly be considered as an FTA partner in future.

In this report, it is shown that Indonesian apparel products tend to face higher tariffs in the U.S. market than its competitors. This is because Indonesian apparel of man-made fiber exports tend to be large and these products face peak tariffs in the U.S. market. Once quotas are eliminated in 2005, it is likely Indonesian apparel exports to the U.S. will be at risk because terms of market access will be determined by tariff levels facing foreign suppliers. Countries with preferential access under FTA or other preferential arrangements are likely to gain market share at the expense of suppliers without such access.

Indonesia will be able to avoid losses through trade diversion if it can improve its productivity and reduce its costs of production enough to offset the Thai margin of preference, but this will be difficult, particularly if the FTAs tend to boost Thai competitiveness by increasing the efficiency of its industries and services. Hence, Indonesia will have to directly tackle the issue of the margin of preference in the Doha Round negotiations by actively seeking to reduce tariff peaks and tariff escalation in the markets of its main trading partners. The prospect for rapid conclusion of the WTO negotiations is rather poor. Hence, Indonesia will need to build its capacity to negotiate bilateral and regional agreements in order to defend the terms of its market access.

Comparative Advantage in Thailand and Indonesia and Thailand's Free Trade Agreements: Potential Diversion of Indonesian Exports

I. Introduction.

The recent trend for Thailand to enter into bilateral free trade agreements (FTAs) with major trade partners outside of the Association for South-East Asian Nations (ASEAN) such as Australia is in marked contrast to Indonesia. The Thai government is second only to Singapore among the ten Southeast Asian nations in the vigorous pursuit of free trade agreements on a bilateral basis with numerous trading partners.[1] The proclivity to negotiate bilateral preferential trade agreements by Thailand is of possibly greater concern to ASEAN partners like Indonesia than is the case with Singapore. Thailand's average MFN tariff for WTO members is 14.6% and its average manufacturing tariff (also for WTO members) is 16.5%.[2] Thailand has bound 74% of its 5,505 tariff lines with the simple average bound rate of 28.4% in 2003.[3] Thailand also maintains tariff quotas on 23 agricultural products (WTO 2003a: 38-39). In contrast, 99.9% of Singapore's tariff lines are duty-free, with only four tariff lines subject to specific duties.[4] Singapore has bound 70.5% of its tariff lines with an average bound tariff rate of 9.7%.[5] The high levels of protection in Thailand compared with Singapore imply larger potential for trade diversion in the Thai case. Preferential agreements between Thailand and major markets for Indonesian exports

[1] Thailand's most recent trade policy review report to the World Trade Organization (WTO 2003a) mentions bilateral FTA negotiations with Australia, Bahrain, Japan, India, Peru, Mexico, New Zealand, South Korea, the United States and China. However, recent press reports indicate Thailand is planning to enter into negotiations with Canada, and Hong Kong as well, for a total of a dozen bilateral agreements. In contrast, Indonesia has yet to enter into formal bilateral FTA negotiations with any trade partner, although it is a member of the ASEAN Free Trade Agreement (AFTA).
[2] These tariff figures are from the WTO (2003b).
[3] See WTO (2003b), 72.1% of the tariff lines are fully bound, with another 1.8% partially bound.
[4] See WTO (2000).
[5] About 55 bound tariffs are specific rather than ad valorem(0.9% of all lines), and 1.9% of all lines are partially bound (WTO, 2000).

like the U.S. and Japan are also of concern because of the potential for such agreements to lead to diversion of Indonesian exports in favor of those of Thailand.[6]

Trade diversion effects of discriminatory preferential trade agreements are not the only source of concern over their proliferation. Investment diversion and the subsequent restriction of intra-industry trade because of rules of origin that exclude intermediate inputs from non-members is another source of worry (Garnaut and Song 2003). The threat of "truncated globalization" is particularly worrisome for East Asia as the recent trade boom fueled by intra-industry trade in components, particularly in electronics and electrical and non-electrical machinery, preceded the formation of the new wave of FTAs involving East Asian entities. If rules of origin are used to restrict members of free trade agreements from using components from non-member sources, this would interfere with firm decisions to locate production facilities in non-members and would further be debilitating to trade by raising costs of production inside the FTA.

II. Free Trade Agreements and the WTO

The World Trade Organization provides for exceptions to the fundamental principle of non-discrimination in the form of free trade agreements under GATT article XXIV, GATS article V and under the so-called "enabling clause" instituted during the Tokyo Round (Srinivasan 1998). The fundamental theoretical debate over whether free trade agreements are "stepping stones" or "stumbling blocks" to global free trade aside, the characteristics of such agreements do matter.[7] Figure 1 is an attempt to develop a simple classification scheme for agreements. The intuition underlying figure 1 is that "WTO-compliant" free trade agreements minimally cover

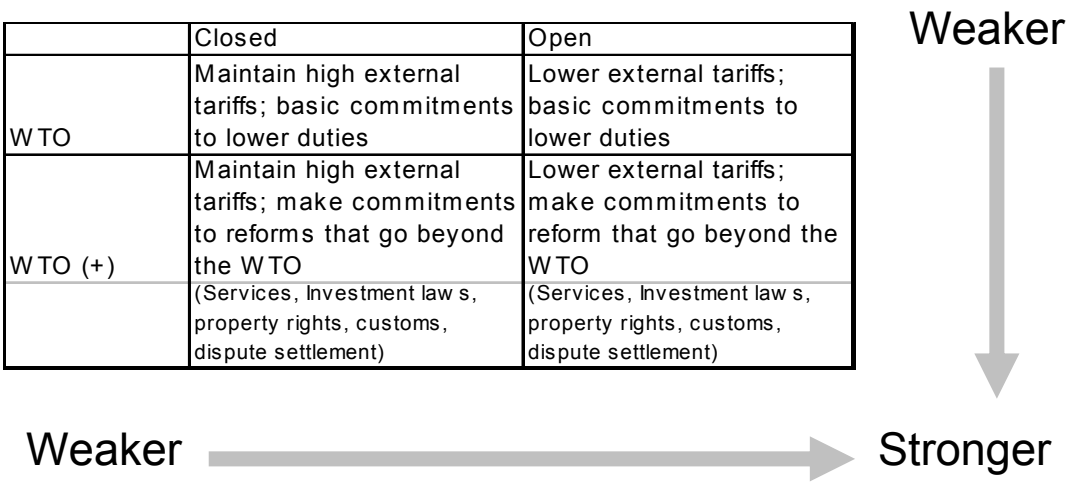
[6] James and Wendel (2004) report a Spearman Rank Correlation Coefficient between imports from Thailand and Indonesia into the US market (excluding values below $0.5 mil.) of 0.643.

[7] For a review of the literature see Panagariya (1999 and 2001).

"substantially all trade", meaning trade in goods with some exceptions (usually for agriculture) and do not raise overall average tariffs on non-members. However, "WTO (+)" free trade agreements are now coming into vogue and go well beyond the minimal requirements in coverage, as suggested in the bottom two quadrants of the matrix.

Figure 1: Classification Matrix for Free Trade Agreements

	Closed	Open
WTO	Maintain high external tariffs; basic commitments to lower duties	Lower external tariffs; basic commitments to lower duties
WTO (+)	Maintain high external tariffs; make commitments to reforms that go beyond the WTO	Lower external tariffs; make commitments to reform that go beyond the WTO
	(Services, Investment laws, property rights, customs, dispute settlement)	(Services, Investment laws, property rights, customs, dispute settlement)



Free trade agreements may be judged to be "closed" or "open" depending on whether they maintain or lower tariff barriers to non-members and whether or not they impose strict rules of origin that lead to reductions in imports of intermediate goods from non-members. Such closed agreements were characteristic of many Latin American trade agreements in the 1970s and recent agreements in Africa and South Asia. NAFTA rules of origin in textiles and automobiles are highly restrictive with respect to intermediate inputs of non-members, but are quite liberal for other machinery sectors, particularly for electronics, telecommunications equipment and computers.[8] Some preferential trade agreements have augmented tariff preferences

[8] Hufbauer and Schott (1993); James and Umemoto (2000) provide evidence of the trade diversion in textiles and apparel from East Asia in the North American markets resulting from the restrictive textiles rules of origin in the NAFTA.

with favorable quota treatment. This is the case in the North American Free Trade Agreement (NAFTA), whereby textile and clothing items produced in Mexico under the "yarn forward" or "triple transformation" rule of origin are free of quotas and pay very low tariffs.[9]

Movement from left to right and from top to bottom in the matrix implies agreements have substantial effects in terms of deepening economic integration between member states. Closed and weak agreements are those that maintain high external tariffs and merely comply with the minimal standards and that lack development of institutions such as dispute settlement mechanisms. Such agreements do little to encourage reform and are mainly political in nature. Open and strong agreements provide support to "lock-in" reforms that liberalize trade and investment and develop strong institutions for resolution of disputes with clear legal guidance and time-bound schedules. NAFTA has been instrumental in Mexico's reform efforts in the areas of trade and customs, financial services and foreign direct investment rules.

Thailand is launching negotiations for a free trade agreement (FTA) with the United States in Honolulu at the East-West Center in late June 2004. There are several reasons for the US-Thai decision to pursue a free trade agreement. A long-term bilateral treaty between the two countries that grants national treatment to U.S. companies that invest and operate in Thailand is due to expire shortly and the U.S. side is keen to preserve this preferential treatment. Thailand is a front-line state in the war on terror and has strongly backed the U.S. in Iraq and Afghanistan by committing Thai troops to the effort. A free trade agreement is one way reward to Thailand for its support in the global fight against the terrorists. None the less, the Thai government's decision to explore the bilateral path to trade liberalization is ironic in that it coincides

[9] See Hufbauer and Schott (l993); James and Umemoto (2000); James (2004) for discussion.

with the term of Thai Director-General Supachai Panitchpakdi as the head of the World Trade Organization (WTO). Thailand states that its bilateral agreements will allow benefits to accrue to third parties yet there are no specifics on the mechanism by which this may occur (WTO 2003b:26).

Table 1. U.S. Import Weighted Tariffs on Apparel in 2001 as % of FOB Value

Customs Territory	Import-Weighted Tariff %	PTA Status
Indonesia	17.5	No
Bangladesh	15.5	No
Pakistan	15.8	No
Malaysia	11.1	No
Thailand	13.7	Negotiations underway
Costa Rica	2.3	CAFTA/CBERA
Mexico	1.3	NAFTA
China	12.0	No
Dominican Republic	3.3	CAFTA/CBERA

Source: USITC 2004

The adoption of rules of origin (or what might more aptly be termed rules of preference) to enforce preferential trade agreements is to exclude benefits from accruing to non-members (third parties) except where exemptions are granted non-members for certain products.[10] The import-weighted average tariff for textile and clothing products in the US market paid by various major suppliers reveals that a preferential arrangement may confer a very substantial margin of preference for products deemed to originate in the territory of a preferential supplier (Table 1). While such arrangements are obviously in the interest of states receiving preferences, they may have adverse consequences for non-members in terms of market access.

Complex rules of origin and overlapping sets of rules of origin (and numerous different preferential tariff rates) may impose substantial costs upon businesses that

[10] For example, the Singapore-US FTA allows duty-free importation of certain Indonesian electronic products produced on Batam Island (a free trade zone). The exemption under the rules of origin is granted to a few specific products that are produced by electronic assembly plants possibly owned by Singaporeans.

are seeking to obtain origin within a preferential trade area. A recent study of the rules of origin in the Australia-New Zealand Closer Economic Relations (CER) agreement by the Australian Productivity Commission (PC, 2003) reveals that compliance with rules of origin could cost between 1-6 per cent of the value of imported goods. Complex and overlapping sets of rules of origin may give rise to customs problems and could lead to corrupt practices in developing countries when the benefits of conference of origin are large.

Free trade agreements have ambiguous effects on global economic welfare and much turns on the details of negotiated outcomes. Empirical evaluations of free trade agreements are best undertaken through *ex post* studies that carefully assess their economic effects on members and non-members.

Open free trade agreements allow member states to use third country intermediate inputs, provided these undergo "substantial transformation" under liberal cumulation clauses. Without provisions allowing Central American countries to use third party inputs, including those from Mexico, the US-CAFTA would be of greatly diminished value to the Central American countries. The African Growth and Opportunity Act (AGOA-3) is set to extend special cumulation rules that enable sub-Saharan African countries to export apparel made from third-country fabric duty-free subject to certain volume limits to the United States for another three years beginning in 2005. Without such a clause and with the end of quotas on January 1, 2005, it is unlikely these countries could maintain a share of the U.S. apparel market.

In the case of preferential trade agreements involving Thailand, rules of origin are likely to be important, as MFN tariffs remain quite high on a number of key industrial and agricultural products in Japan and the United States. Possible trade

diversion impacts of new free trade agreements between Thailand and the US and Thailand and Japan are explored in the following sections.

III. Comparative Advantage in Thailand and Indonesia

Comparative advantage has evolved rapidly in newly industrializing economies of Asia and Thailand and Indonesia are no exceptions. Evolution over the past fifty years has seen comparative advantage shift from primary exports of logs, minerals, fish and agricultural commodities, to processed products such as plywood, metals, canned fruit and fish, and prepared food products, to light manufactures of footwear, textiles and clothing and toys, and finally, to electrical machinery, office and computing equipment and transportation equipment. In some industries, comparative advantage is sustainable for relatively long periods (e.g., textile and clothing sectors, minerals and plantation crops such as natural rubber). However, careful analysis of major manufacturing exports reveals that comparative advantage is rapidly being transformed as educational levels rise and as foreign investment and intra-industry trade link these economies to the global markets. Indeed, multinational enterprises have played a key role in structural transformation of the manufacturing industries in these two economies.[11]

Table 2: Trade with the World and Revealed Comparative Advantage (period averages, annual totals)

Country, commodity group	1985-87	1988-90	1991-93	1994-96	1997	1998	1999	2000	2001
REVEALED COMPARATIVE ADVANTAGE INDICES									
Indonesia									
Manufactures	0.348	0.485	0.664	0.685	0.565	0.569	0.700	0.757	0.750
Textiles	0.891	1.292	2.055	1.822	1.243	1.361	1.805	1.749	1.714
Apparel	2.040	2.732	3.289	2.416	1.813	1.836	2.897	3.000	3.216
Nonelectric machinery	0.010	0.015	0.035	0.075	0.080	0.139	0.136	0.180	0.149
Office & computing mach.	0.017	0.012	0.096	0.371	0.550	0.533	0.854	1.846	1.380
Other electric machinery	0.050	0.058	0.274	0.475	0.429	0.386	0.422	0.646	0.729
Transportation machinery	0.007	0.018	0.069	0.093	0.068	0.113	0.091	0.082	0.082
Thailand									
Manufactures	0.689	0.784	0.906	0.949	0.929	0.931	0.941	0.986	0.973
Textiles	2.017	1.492	1.085	1.079	2.887	2.818	2.648	2.588	2.540
Apparel	3.273	3.674	3.536	2.653	2.072	2.215	2.141	2.127	2.172
Nonelectric machinery	0.176	0.208	0.352	0.448	0.501	0.484	0.524	0.574	0.597
Office & computing mach.	0.301	1.287	2.123	3.254	4.044	4.834	4.882	4.773	4.656
Other electric machinery	0.998	1.148	1.446	1.413	1.416	1.430	1.400	1.457	1.448
Transportation machinery	0.028	0.065	0.135	0.244	0.255	0.194	0.285	0.334	0.367

Source: James and Ramstetter (2004).

Comparative advantage in Thai and Indonesian manufacturing industries, represented by revealed comparative advantage (RCA) indices over the period of 1985-2001, has undergone some change (Table 2). Both countries kept a revealed comparative advantage in the apparel sector over the entire period. Yet, it appears that Indonesia has become relatively more competitive in apparel than Thailand in the period since the financial crisis of 1997-98. Both countries have also maintained a revealed comparative advantage in textiles over the entire period for Thailand and since 1988 for Indonesia. The major change is in office & computing machinery with both countries attaining a revealed comparative advantage by year 2000, with Thailand achieving this more than a decade earlier than Indonesia. Thailand also has a revealed comparative advantage in other electrical machinery since 1988.

[11] Ramstetter1991, James and Ramstetter (1997 and 2004)

Market shares and growth are key indicators of export competitiveness, which is also affected by supply-side factors in addition to external demand conditions. Clearly, on the demand side, terms of market access may strongly influence performance in market share and growth because market access conditions will directly or indirectly affect the prices of the products imported from various sources compared with prices of domestically produced goods. If Indonesian exports are taxed more heavily than those of competitor's, then Indonesian producers will have to cut costs or they will lose market share, given normal profits and assuming no or little change in real exchange rates.[12]

Indonesia's export competitiveness in its two largest markets, the United States and Japan, was evaluated over the period of 2001-2003 using quarterly import data from official sources in both the U.S. and Japan. The advantage of using import data is that these data are more accurate and timely than the data from the exporting country. Performance of the top 50 SITC 3-digit products in the two largest markets was examined over the most recent three years, with the products being the top Indonesian non-oil exports to the U.S. and Japan, as recorded in these countries' import data. In the case of Japan, the top 50 products accounted for over 89% of total Indonesian non-oil exports in 2003. In the case of the U.S., these products accounted for over 92% of U.S. non-oil imports from Indonesia in 2003.

[12] Market share in this exercise refers to the share of total imports of a 3-digit SITC category coming from Indonesia versus other customs territories. This approach abstracts from domestic production and is less comprehensive than market share measured as imports over domestic apparent consumption. However, import market share is available for 2003, whereas market share of apparent consumption can only be calculated through 1998 or 1999.

Table 3. Japan Imports of Top Indonesian Non-Oil Products in 2003 (current prices, Millions of US$)

SITC and Description	Imports from Indonesia	Imports from Thailand
036 Custaceans	486.4	317.9
288 Nonferrous Base Metal & Scrap	365.3	18.2
641 Paper and Paperboard	296.1	22.1
752 Automatic Data Process Mach.	223.7	245.3
231 Natural Rubber	223.6	525.3
821 Furniture & Bedding	207.0	329.0
763 Sound and TV Recorders	200.4	80.3
651 Textile Yarn	185.5	61.6
776 Thermionic Cold Cathode	168.2	694.8
764 Telecommunications Equip.	152.2	481.1
034 Fresh Fish	150.5	231.6
037 Fish, Crustaceans and Molluscs	148.7	391.1
773 Equip. for Distributing Elec.	148.3	156.3
635 Wood Manufactures	138.4	48.9
771 Electric Power Mach. & Parts	108.8	109.6
851 Footwear	103.1	54.3
778 Elec. Machinery & Appar.	99.6	188.0
574 Polyacetals & Epoxide Resins	96.0	26.9
893 Articles of Plastics	91.6	171.6
772 Elec. Appar. for Switching	88.2	274.2
761 Television Receivers	84.1	79.5
784 Parts of Motor Vehicles	83.1	208.7
716 Rotating Electric Plant & Parts	77.7	79.4
625 Rubber Tires & Accessories	73.3	43.0
642 Paper & Paperboard Cut to Size	65.4	16.8
713 Internal Combustion Engines	64.7	56.6
512 Alcohols, Phenols & Deriv.	63.1	24.5
000 Unclassified Products	59.8	529.9
687 Tin	57.5	21.4
667 Pearls, Precious Stones	56.5	66.1
582 Plates Foil & Strip of Plastics	54.4	17.1
841 Men's Boy's Coats, Not Knit	44.9	42.0
653 Manmade Woven Fabrics	44.1	12.9
775 Household Type Elec. Equip.	42.4	384.1
699 Manufactures of Base Metal	36.1	95.1
598 Miscellaneous Chemicals	34.9	82.4
658 Made-Up Articles of Textiles	33.9	12.7
845 Articles of Apparel	32.8	77.7
759 Parts for Office Mach.	31.9	152.9
652 Cotton Fabrics, Woven	30.5	8.1
TOTAL	**4,752.7**	**6,439.0**

Source:James and Minor (2004).

In the U.S. case, of the 50 top products in 2003, import market share fell in 23 cases, was unchanged in 11 and rose in 16. In Japan, import market share fell in 22 cases and rose in 22 cases while in 6 cases it remained unchanged.[13] Upon examination of the results, it was found that Thailand competes directly with Indonesia in many of these products in both the U.S. and Japan. An evaluation of the products with which Thailand is a major competitor with Indonesia is provided for the most recent year, 2003 (Tables 3 and 4).

In Japan (table 3) imports from Indonesia and Thailand are concentrated in natural resource-based industries, including minerals, fisheries and forestry products. Of the fifty top items imported from Indonesia, 40 directly compete with similar products from Thailand (80%). Japan's imports are still relatively heavily concentrated in natural resource-based items. For example, in 2003 19 of the top 50 imports from Indonesia are in these resource-based sectors, 14 of which are subject to competition with similar Thai products. Thailand does not export the following products of interest to Indonesia to Japan: copper, aluminum, plywood and wood, and coffee. Indonesia and Thailand compete in six textile and apparel product groups in Japan. In 2003, these product groups accounted for $371.9 million in export receipts for Indonesia and $215.0 million in Thailand. From these data, we estimate trade diversion from Indonesia to Thailand under a Japan-Thai FTA to have the potential to affect trade with a value in the range of $4-5 billion. Further analysis of trade barriers and the margin of preference offered to Thai producers would be necessary to more rigorously estimate the likely range of trade diversion. In addition, sector and product

[13] This summarizes the results of a comprehensive study of market shares of Indonesian non-oil exports in these two large markets (James and Minor 2004). The import market shares of Indonesia and its 15 top competitors are evaluated over the course of 2002-2003 in this study. A previous study did the same comparing 2001 and 2000 data (James 2002). All these data are available from the author upon request.

specific rules of origin applied to auto parts and electronic components could lead companies to divert investment in production facilities and eventually to divert trade in components from Indonesia to Thailand and stifle the future development of components trade with Indonesia.

In the United States (table 4) of the top 50 imports from Indonesia, 28 compete directly with similar Thai products (56%). U.S. imports are heavily concentrated in textile and apparel manufactures with ten items in the top 50 from Indonesia, eight of which Thailand is a major competitor in. These textile and apparel items accounted for $2,751.9 million in export receipts for Indonesia in 2003 and $2,797.1 million for Thailand. This presents a huge trade diversion potential as the average import weighted tariff on these textile and apparel items from Indonesia is nearly 18% for clothing and 10% for textiles.[14] If Thai products gained duty-free access after quotas are eliminated next year, there would be a very large margin of preference in Thailand's favor. Overall, the maximum potential for trade diversion from Indonesia should there be a Thai-US FTA is $6.3 billion (table 4). Again it is important to examine tariff and non-tariff barriers to assess more rigorously the actual likelihood for trade diversion in the US market.

Clearly, it is not possible to *a priori* forecast trade diversion from a free trade agreement with any precision. This is why *ex post* rather than *ex ante* studies are necessary to accurately assess the benefits and costs of such trade agreements. While this issue cannot be settled for several years, it is important for countries like Indonesia to recognize that much is at stake, even if the precise amount of "much" is not known.

[14] See USITC (2004).

Table 4. U.S. Imports of Top Indonesian Non-Oil Products in 2003 (current prices, Millions of US$).

SITC and Description	Imports from Indonesia	Imports from Thailand
842 Women's/Girl's Coats, not	836.3	413.0
845 Articles of Apparel of	616.4	753.2
231 Natural Rubber	595.9	258.0
851 Footwear	569.6	284.7
763 Sound & Television	552.1	336.3
821 Furniture & Bedding	524.4	412.0
752 Automatic Data Process	338.7	1,659.4
762 Radiobroadcast Receivers	171.0	148.0
036 Crustaceans	169.1	597.7
894 Toys & Sporting Goods	163.2	295.2
037 Fish, Crustaceans & Mollusks	154.9	772.8
776 Thermionic Cold Cathodes	141.1	616.4
635 Wood Manufactures	127.0	138.5
034 Fresh Fish	106.7	53.7
843 Men's/Boy's Coats Knitted	93.6	218.1
761 Television Receivers	86.3	664.4
759 Parts for Office Mach.	83.8	262.2
848 Apparel & Access. Headgear	80.7	413.8
773 Equip. for Distributing Elec.	80.5	174.4
897 Jewelry, Gold & Silver Ware	69.5	806.5
831 Trunks, Suitcases	68.1	114.5
574 Polyacetals & Epoxide Resins	56.0	115.3
697 Household Equip. Base Metal	47.8	205.6
658 Made-Up Articles of Textiles	47.4	142.8
666 Pottery	46.7	81.8
652 Cotton Fabrics, Woven	46.3	41.7
893 Articles of Plastics	44.7	133.1
662 Clay & Refractory Cons.	33.5	21.8
TOTAL	**5,951.3**	**10,134.9**

Source: James and Minor (2004).

IV. Implications for Indonesia

Thomas Friedman (2002:4) points out: "whether you are a company or a country, your threats and opportunities increasingly derive from who you are connected to." In the game of trade negotiations, being connected to the big markets through free trade agreements is becoming more and more important. With the demise of the global system of textile quotas in the coming year, preferential market access could be a crucial determinant of export performance and industry profitability. This seems to help explain the vigorous pro-active efforts of Singapore and Thailand

in securing free trade agreements with major trade partners and the largest markets. If one evaluates the risks faced by not acting, the scramble to negotiate seems logical.[15]

From an Indonesian perspective, then, it follows that if Thailand succeeds in negotiating free trade agreements with Japan and the US, nearly $10 billion in non-oil exports would be at risk from enhanced Thai competitiveness in these markets. The immediate implication is that Indonesia has to consider various options as major competitors enhance their market access terms in the major world markets. If Indonesia is unable to come to the negotiating table, it will have to greatly improve its supply chain performance to cut costs in order to compete. It will also need to enhance services, which is one of the main advantages of joining into FTA arrangements with advanced economies in the first place.

A first-best solution would be for the Doha Round to succeed in cutting peak tariffs on products of export interest to Indonesia, but this may be several years in the offing. If that is the case, creative solutions might be sought under existing regional or bilateral arrangements to improve market access in addition to efforts to improve supply-side efficiency.

[15] James and Minor (2004) provide an assessment of the risk facing various Southeast Asian apparel exporters once quotas are lifted on January 1, 2005. It turns out that Thailand faces greater risk than Indonesia and this may help explain the differences in negotiating positions.

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